

CLEVELAND PUBLIC LIBRARY
BUSINESS INF. BUR.
CORPORATION FILE

Food Fair Stores, Inc. 1976 Annual Report



A MEMORIAL TRIBUTE

to
Myer B. Marcus

In a distinguished career that spanned 47 years, Myer B. Marcus was a major force and tower of strength in the growth and progress of Food Fair Stores, Inc.

A man of vision with a keen, inquisitive mind and selfless dedication, he played a key role in the launching of the Company's first supermarket in 1933 and in the subsequent development of the Company into the position of eminence it holds today as a leader in the retail food field.

To all of the increasingly responsible positions he held through the years, as Director of Store Operations, Vice President, Executive Vice President, Vice Chairman and Chairman of the Board, he brought to bear perceptive insight, analytical judgment and sound business acumen which proved invaluable in corporate policy decision making.

He had within him the restless spirit of one never satisfied with what had been accomplished but relentlessly striving for improvement, always seeking new, higher goals.

This spirit was most notably reflected in the self-service innovations he pioneered: from the shopping cart and a white spot on food packages for price marking to the design and decor of the modern supermarket consumers have grown accustomed to expect.

Through his services as an Officer and Director of the National Association of Food Chains, the Super Market Institute, and as President and Director of the International Association of Food Chains, he gave generously of his time and unique abilities to further the growth and development of the supermarket industry.

His concern for the development of future industry executives was manifest in the role he played as founding Chairman of the Academy of Food Marketing at Saint Joseph's College, Philadelphia, recognized today as one of the outstanding educational centers for young persons eager to pursue careers in the food industry.

While serving with distinction in demanding and challenging positions with his Company and industry, he nonetheless was an active participant and leader in a host of communal and charitable activities.

For all those qualities he possessed from which came the invaluable contributions he made to his Company, the food industry and the community, the Board of Directors record with profound sorrow their loss at the passing on July 20, 1976, of their respected colleague and friend, Myer B. Marcus, Chairman of the Board.

Resolution Adopted by the Board
of Directors, August 9, 1976.



Myer B. Marcus

Cover

Planning for growth. The Company has developed a new five-year plan that calls for an acceleration in both new store openings and the remodeling of existing units. The plan, initiated with the current fiscal year, is discussed in the Letter to Shareholders.

Our Business

Food Fair Stores, Inc. is one of the nation's largest diversified retail chains with 443 supermarkets and 82 discount department stores serving consumers in 14 eastern seaboard states from New Hampshire to Florida.

The Company is also engaged in the manufacture and processing of foods for sale in its stores as well as to others, and has several non-food related operations.

In addition, the Company owns 40% of the common stock and all of the preferred stock of Amterre Development Inc., a large owner and developer of shopping centers and other real estate properties.

Annual Meeting

The annual meeting of shareholders will be held Tuesday, November 16, 1976, at 2 P.M., local time, in the Bellevue Stratford Hotel, Broad and Walnut Sts., Philadelphia. Shareholders are cordially invited to attend. A notice of the meeting, a proxy statement and proxy form are included with this report to each shareholder of record as of October 13, 1976.

Form 10-K

A copy of Form 10-K for the fiscal year ended July 31, 1976, which has been filed with the Securities and Exchange Commission, is available to shareholders at no charge upon written request to: Office of the Corporate Secretary, Food Fair Stores, Inc., 3175 J. F. Kennedy Boulevard, Philadelphia, PA 19101.

Common Stock Traded

New York Stock Exchange
PBW Stock Exchange

Letter to Shareholders

I am pleased to report a significant improvement in your Company's performance in fiscal 1976. Earnings of \$6.6 million, equal to 88 cents a share, were achieved from continuing operations, compared with a loss of \$3.2 million from continuing operations in the previous year. The improvement can be attributed in large part to the encouraging turnaround achieved by our discount department stores and the increased profitability of our supermarkets.

In 1976, a loss of \$2.7 million was sustained in the Company's investment in Amterre Development Inc, a 40% owned unconsolidated subsidiary. This loss has been reported as a loss from discontinued operations of an unconsolidated subsidiary and reduced the net income to \$3.8 million, compared with a net loss of \$3.4 million in fiscal 1975.

Four new supermarkets were opened during the year and nine other

food units were remodeled, including two which were enlarged and four which were converted to discounting operations under the Pantry Pride name. Twenty supermarkets and three J. M. Fields discount department stores were closed. At fiscal year end, there were in operation 443 supermarkets and 82 discount department stores.

An upturn in the nation's economy and a slowing of the inflation rate buoyed consumer confidence and stimulated greater discretionary spending which had been severely restricted during the recession. This was especially beneficial to our department store operations and enabled an increase in gross margins which had been severely depressed.

Despite increased competitive pressures, your Company successfully maintained its sales volume even with 17

fewer supermarkets and three fewer discount department stores in operation at fiscal year end than the year before. Sales were \$2.50 billion compared with \$2.48 billion the prior year.

In recent years, your management has followed a selective new-store development program, concentrating primarily on conversion of supermarkets to a discount pricing format, which has significantly increased average store sales. Older, smaller units incapable of generating the sales and profitability required for successful conversion to discounting have been closed.

We have recently completed an intensive study of our present retailing facilities as part of our continuing review and assessment of operations required to chart future growth. This most recent study, which examined each of our units and measured their future viability against many criteria, has provided the



foundation for a five-year development program now under way. Like any plan it will be reevaluated on a periodic basis for the continued validity of its assumptions and in view of attainment of sales and profit goals.

The plan calls for an acceleration in the building of new supermarkets, averaging 33,500 square feet, the refurbishing and expansion of existing units with demonstrated potential for growth and the closing of units which do not offer the promise of longer-term profitability. The concentration of new stores and improvements to existing stores will be in our major marketing areas where we have a strong identification and consumer support.

In the current fiscal year, eight new stores are planned, compared with four that opened in fiscal 1976, while some 30 stores are scheduled for remodeling, expansion or conversion to discounting operations, more than triple the number in fiscal 1976.

The plan contemplates improvements of all stores on a regularly scheduled basis to insure a continuity of modern, efficient retailing facilities. It is expected that this capital program will be financed largely through internally-generated funds.

The major concentration in J.M. Fields will be on building sales and profitability within existing units. No new stores are presently planned for fiscal 1977.

The emphasis in our manufacturing and processing operations will be on increasing the sales of products currently in production and selective addition of new products.

The five-year plan is well within our capabilities of accomplishing. It is fiscally sound and based on realistic, conservative assumptions.

In recent weeks we signed an agreement to acquire 17 Penn Fruit supermarkets, all located in the greater Phila. area, which will strengthen our position in this key market, and is consistent with our plan to expand in those areas where we are already well entrenched. Fourteen of these stores are in current operation and three units, presently closed, will be reopened shortly.

In planning for the growth of the supermarket division, by far the largest of our major divisions, the Directors elected Frank N. James a corporate vice president, and named him to the new post of president of the Pantry Pride Supermarket Division. Mr. James, formerly supermarketing vice president for the Philadelphia Region, will be responsible for all of the Company's supermarket operations. Marvin Lerner, supermarketing vice president for the Southern Region, was promoted to executive vice president of the Pantry Pride Supermarket Division. Both are seasoned supermarket executives.

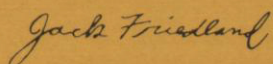
Harold Friedland, a corporate vice president and director, has advised the Board of Directors that for reasons of health he did not wish to stand for reelection as a director at the annual meeting in November and will resign from the Company at that time. Mr. Friedland has served the Company for more than 25 years in a number of increasingly responsible store operations and merchandising posts. The directors accepted with regret Mr. Friedland's decision and express to him their appreciation for his many years of dedicated service.

Howard F. Gordon was elected corporate secretary at the first meeting of directors convened after the annual meeting last year. Mr. Gordon, the Company's corporate counsel, succeeded B.F. Lieber, who retired after 40 years of meritorious service.

In February, 1976, Willard S. Boothby, Jr., chairman and chief executive officer of Blyth Eastman Dillon & Co., Inc., was elected a director. Mr. Boothby succeeded D. Frederick Barton of the same firm who served with distinction as a director since 1957 and is now retired.

In closing, I take note with sorrow of the death on July 20 of Myer B. Marcus, chairman of the board, who gave 47 years of distinguished service and leadership to the Company. Mr. Marcus' contributions to the Company and his personal qualities are reviewed in the memorial tribute to him on the inside cover of this report. He will be deeply missed by those privileged to have known him and benefited from his counsel and guidance.

Sincerely,



Jack Friedland
President
Chief Executive Officer



Jack Friedland



October 28, 1976

Pantry Pride Supermarket Division

The Pantry Pride Supermarket Division maintained its sales volume and increased its operating profit despite intensified competition and having 16 fewer stores in operation at year end. Aggressive merchandising, effective cost controls and improved productivity contributed to the results.

Four new supermarkets, averaging 31,500 square feet, were opened, three in South Florida and one in New Jersey. Nine food stores were remodeled and 20 older units were closed. With few exceptions, the conversion of the Company's 443 supermarkets to discounting operations has been completed. The remaining conventional food units will be converted to discounting in fiscal 1977.

In an organizational realignment for more effective operation, the 20 stores comprising the Connecticut Branch were merged into the New York Branch and Linden Region. Four outlying stores in upper New York state were sold consistent with the Company's intention to concentrate its growth in areas where it is well established.

Employee training programs placed renewed emphasis on customer service



and courtesy. These "intangibles" were also the basis of a number of themes featured in newspaper ads. For example, a "Feel Good" campaign conducted in many operating areas was aimed at increasing employee sensitivity to the importance of efficient, courteous service to consumers.

At the same time, the Supermarket Division's commitment to personnel development and training, particularly at the middle and upper management levels, was reinforced with the appointment of Herbert Zandler as vice president-human resources, a new post. Mr. Zandler, formerly supermarketing vice president for the Baltimore Region, is responsible for the initiation and coordination of programs to assure a reservoir of qualified personnel to fill key management posts.

In other personnel appointments, Albert Faraldi, New York branch manager, and Robert U. Ochsenhirt, West Coast Florida branch manager, were promoted to assistant vice president in their respective areas.

Consumer affairs programs were expanded to involve greater numbers of shoppers with the establishment of consumer boards at the store level as well as at the regional level. In this broadened concept, a store manager and his staff will meet regularly with a consumer board selected from the store's own shoppers. These boards represent a cross section of supermarket shoppers who meet with operating management to exchange views, air grievances and offer constructive criticism.

Consumer education programs were also continued, which included the preparation and distribution of information related to food shopping, nutrition, budgeting, meal planning and health. Consumer affairs personnel made frequent appearances on radio and television programs and before various groups.

Electronic and computer technology is being utilized increasingly to improve efficiency at all steps in the food distribution system . . . from truck deliveries to warehousing to store ordering to checkout. The first full-scale use of electronic scanning at the checkout will be tested shortly at a store in Moorestown, N.J. This system automatically records the price and description of the item as the cashier passes the product

over an electronic scanner. The system offers tremendous potential for more efficient checkout service and more effective management decision-making. Several other tests are planned in 1977.

Electronic technology is also being utilized in reducing energy costs. Demand control mini-computers have been installed in various Company locations. These units automatically turn equipment on and off based upon need and a pre-established peak limit. They prevent usage from exceeding the peak limit. This results in reduced utility expense since costs are based on peak demand and kilowatt usage. Test results indicate a 10% to 20% reduction in utility costs can be effected with the widespread introduction of these computers to other areas of the Company.

Other steps taken to save energy costs include heat recovery and cold air recapture systems. Heat recovery systems recapture gases from refrigeration equipment and pipe them back in as heat, resulting in a substantial savings in fuel oil purchases. These systems are being installed in all new and remodeled stores. Mechanical systems are also being redesigned for new stores to facilitate the recapture of cold air from refrigerated cases. This technique reduces air-conditioning requirements and costs.



J. M. Fields

The discount department store division reduced its operating loss by almost 70% and achieved a 4% sales increase, even with three fewer units in operation at year end.

Improved gross margins, increased sales of more profitable merchandise and more effective control of operating costs contributed to the results.

Major emphasis has been on upgrading of merchandise, particularly women's ready-to-wear and fashion goods, and development of improved distribution and store ordering systems.

Consumer acceptance of the upgrading has been most encouraging and the program will be broadened to other apparel lines.

In addition, J.M. Fields has benefited from more sophisticated controls for monitoring sales and managing inventories. This has been particularly beneficial in the rapid, basic replenishment of hardlines and softlines. A new computerized reordering program allows headquarters personnel to carefully



screen reorders by store to insure adequate stock-on-hand.

Several test programs were launched last year to improve store profitability. In 37 stores, group managers with responsibility for several related departments have been designated, rather than having managers for individual departments. Under this program, a personnel/consumer relations specialist has been added to the store manager's staff to handle non-sales related duties, thus freeing the store manager and group managers to concentrate their efforts on merchandising. The personnel/consumer relations specialist is responsible for scheduling, training and development of employees and improving customer service with special emphasis on expediting checkout procedures.

A second program focused on the profitable growth of 16 smaller-volume stores. Elements of this program included a reduction in merchandise assortment, consistently low prices on a select group of items and increased special promotions.

In addition, profitability studies are being conducted to ascertain those merchandising areas which can yield greater gross margin dollars per square foot. Assortment plans are also continually reviewed in order to maximize profit. Similarly, the aging of merchandise is monitored through dated tickets on all goods. Programs are developed for the most profitable movement of this merchandise.

Three J.M. Fields stores, in Swampscott, Mass., Delran, N.J., and Anderson, South Carolina, were closed during the year.

In fiscal 1977, primary efforts will be concentrated on the expansion of sales within existing units.

A number of key promotions were made during the year.

Ralph Blumenstock, formerly vice president-softlines merchandise manager, was promoted to senior vice president-marketing, advertising and general merchandise manager.

Robert M. Hunt, senior vice president, sales and operations, was named to act as general manager.

Oscar Kettler, formerly general merchandise manager-hardlines, was promoted to vice president, general merchandise manager-hardlines. Jack Rule, formerly director, major appliances and electronic sales, was promoted to vice president and general manager, major appliances and electronic sales.

Ideal Shoe Company

Ideal Shoe Company operates leased shoe departments in 93 discount department stores. These shoe departments offer economy and value in footwear for all members of the family. While a substantial portion of the total sales is generated from departments in J.M. Fields stores, the company has been concentrating its expansion efforts with non-affiliated chains. Towards this goal the company recently opened six new departments. Ideal Shoe will also test a free-standing, self-service store, which is expected to open late in 1976.

The company purchases the bulk of its merchandise on a direct contract basis from both domestic and foreign manufacturers, and operates its own 110,000 square foot distribution center in Philadelphia.



Manufacturing & Processing

The Company operates three bakeries, a beverage plant, a coffee roasting plant, two meat slaughtering plants and several other manufacturing and processing operations. These facilities supply products to Company outlets and service outside customers as well.

The Company is committed to the development of private label products comparable in quality to competitive national brands. Consistent with that policy, our own manufactured items are subjected to exacting quality control standards. They sell for less than comparable national brands, are more profitable and enjoy excellent consumer acceptance.

In addition, private label products made for us by other manufacturers also must meet the quality standards we establish, and their facilities are regularly inspected by our quality control staff members.

Samples of every shipment of private label merchandise are forwarded upon receipt at our distribution centers for quality control tests to assure they meet specifications. Private label products

are continually taste-tested and kitchen-tested by our staff of home economists.

New additions considered for the private label line also must undergo extensive testing, development and product specification analysis.

Private label packaging has been redesigned and now provides a distinctive quality look, along with the valuable nutrition information, often more comprehensive than required by law.

Selected new additions to our line of manufactured products are planned in fiscal 1977. However, major emphasis will be placed on further increasing sales of products currently in production.



Five Year Summary of Operations

Food Fair Stores, Inc. and Subsidiaries

| | Year ended | | | | |
|----------------------------------------------------------------------------------|--------------------------------|---------------------------------|---------------------------------------------------|--------------------------------|--------------------------------|
| | July 31, 1976 (52 weeks) | August 2, 1975 (52 weeks) | August 3, 1974 (53 weeks) (in thousands) | July 28, 1973 (52 weeks) | July 29, 1972 (52 weeks) |
| Income: | | | | | |
| Sales | \$2,507,040 | \$2,482,539 | \$2,369,761 | \$2,092,127 | \$1,980,458 |
| Equity in earnings of unconsolidated subsidiaries | 611 | 1,150 | 1,484 | 974 | 951 |
| Gain on debentures purchased for sinking fund | 697 | 290 | 282 | 384 | 329 |
| Other | 5,622 | 2,302 | 1,930 | 817 | 496 |
| | <u>2,513,970</u> | <u>2,486,281</u> | <u>2,373,457</u> | <u>2,094,302</u> | <u>1,982,234</u> |
| Costs and expenses: | | | | | |
| Costs of sales | 2,010,399 | 2,006,177 | 1,905,937 | 1,699,929 | 1,611,094 |
| Operating, general and administrative expenses | 482,258 | 473,535 | 442,452 | 374,057 | 352,165 |
| Interest | 11,513 | 13,831 | 11,833 | 12,018 | 8,196 |
| | <u>2,504,170</u> | <u>2,493,543</u> | <u>2,360,222</u> | <u>2,086,004</u> | <u>1,971,455</u> |
| Income (loss) from continuing operations before income taxes | 9,800 | (7,262) | 13,235 | 8,298 | 10,779 |
| Income taxes (benefits) | 3,224 | (4,036) | 4,175 | 1,954 | 3,704 |
| Income (loss) from continuing operations .. | 6,576 | (3,226) | 9,060 | 6,344 | 7,075 |
| Loss from discontinued operations | 2,748 | 208 | 134 | 182 | 5,524 |
| Income (loss) before extraordinary items .. | 3,828 | (3,434) | 8,926 | 6,162 | 1,551 |
| Extraordinary items | | | | (4,031) | (2,949) |
| Net income (loss) | <u>\$ 3,828</u> | <u>(\$ 3,434)</u> | <u>\$ 8,926</u> | <u>\$ 2,131</u> | <u>(\$ 1,398)</u> |
| Income (loss) per share of common stock: | | | | | |
| Continuing operations | \$.88 | (\$.45) | \$ 1.20 | \$.82 | \$.92 |
| Discontinued operations | (.37) | (.03) | (.02) | (.02) | (.73) |
| Income (loss) before extraordinary items | .51 | (.48) | 1.18 | .80 | .19 |
| Extraordinary items | | | | (.53) | (.39) |
| Net income (loss) | <u>\$.51</u> | <u>(\$.48)</u> | <u>\$ 1.18</u> | <u>\$.27</u> | <u>(\$.20)</u> |
| Weighted average number of common shares outstanding during the year | <u>7,360,801</u> | <u>7,380,145</u> | <u>7,508,754</u> | <u>7,556,211</u> | <u>7,556,378</u> |
| Cash dividends per share: | | | | | |
| Common share | <u>\$.20</u> | <u>\$.20</u> | <u>\$.20</u> | <u>\$.20</u> | <u>\$.55</u> |
| Preferred share | <u>\$ 4.20</u> | <u>\$ 4.20</u> | <u>\$ 4.20</u> | <u>\$ 4.20</u> | <u>\$ 4.20</u> |

Management Analysis of Operations

1976 compared with 1975

Supermarkets

Operating profit rose by \$1.5 million to \$32.4 million despite intensive competition in major marketing areas.

Gross profit increased approximately \$8 million, attributable chiefly to the stabilization of food prices and the absence of costly work stoppages which occurred in 1975.

Selling, general and administrative expenses increased \$6.5 million or approximately 2%, reflecting tight controls on labor, and store occupancy costs, particularly utility expenses.

Supermarket sales remained relatively constant even with 16 fewer stores at fiscal year end. However, average store sales of those supermarkets in operation throughout the year increased 3.4%.

Discount Department Stores

Improved gross margins, increased sales and effective controls over general, selling and administrative costs contributed to the substantial reduction in the discount department stores division operating loss to \$5.8 million from \$18.2 million.

Sales rose by 4% to \$324 million, even with three fewer stores in operation at year end.

Gross profit increased \$10.5 million and general, selling and administrative costs were reduced by \$2 million.

Interest

Interest expense was reduced \$2.4 million. Overall borrowings, both short-term and long-term, declined in 1976. Long-term debt decreased by \$7.8 million and average short-term loan balances by \$4.2 million (\$28.6 million vs. \$32.8 million in 1975). This reduction, coupled with a lower average short-term interest rate of 7.2% vs. 9.2% in 1975 accounted for the lower debt expense.

Discontinued Operations of Unconsolidated Subsidiary

The loss of \$2.7 million represents the Company's equity in the loss of Amterre Development Inc, sustained as a result of the transfer of certain property to the mortgagee in satisfaction of first mortgages on the property. This transaction is more fully described in Note 4 to the consolidated financial statements.

Quarterly Data

| Quarter | Total Sales (Thousands) | | Net Earnings Continuing Operations (Thousands) | | Earnings Per Share | | Loss on Discontinued Operations (Thousands) | | Earnings Per Share | | Net Earnings (Thousands) | | Earnings Per Share | |
|----------------|----------------------------|--------------------|------------------------------------------------------|------------------|-----------------------|----------------|---------------------------------------------------|----------------|-----------------------|----------------|-----------------------------|------------------|-----------------------|----------------|
| | 1976 | 1975 | 1976 | 1975 | 1976 | 1975 | 1976 | 1975 | 1976 | 1975 | 1976 | 1975 | 1976 | 1975 |
| 1st (16 weeks) | \$ 756,553 | \$ 758,407 | \$1,661 | \$2,338 | \$.22 | \$.31 | — | — | — | — | \$1,661 | \$2,338 | \$.22 | \$.31 |
| 2nd (12 weeks) | 617,499 | 575,354 | 1,829 | (518) | .25 | (.07) | — | — | — | — | 1,829 | (518) | .25 | (.07) |
| 3rd (12 weeks) | 583,988 | 569,039 | 1,581* | (6,670) | .21* | (.90) | (2,748)** | — | (.37) | — | (1,167) | (6,670) | (.16) | (.90) |
| 4th (12 weeks) | 549,000 | 579,739 | 1,505 | 1,624 | .20 | .21 | — | (208)** | — | (.03) | 1,505 | 1,416 | .20 | .18 |
| Total Year | <u>\$2,507,040</u> | <u>\$2,482,539</u> | <u>\$6,576</u> | <u>(\$3,226)</u> | <u>\$.88</u> | <u>(\$.45)</u> | <u>(\$2,748)</u> | <u>(\$208)</u> | <u>(\$.37)</u> | <u>(\$.03)</u> | <u>\$3,828</u> | <u>(\$3,434)</u> | <u>\$.51</u> | <u>(\$.48)</u> |

*To conform with the position of the Securities & Exchange Commission, this amount has been restated to reflect a deferral over future periods of \$1.2 million, or 16 cents a share, of the gain on the RMC transaction. See Note 6 to the consolidated financial statements.

**See Note 4 to the consolidated financial statements.

Operating Results by Lines of Business

Food Fair Stores, Inc. and Subsidiaries

Year Ended Nearest July 31:

| | 1976 | 1975 | (53 weeks) 1974 | 1973 | 1972 |
|------------------------------------------------------------------------|------------------|------------------|--------------------|------------------|------------------|
| | (\$ in millions) | | | | |
| Sales: | | | | | |
| Supermarket operations: | | | | | |
| Continuing | \$1,962.3 | \$1,966.3 | \$1,893.6 | \$1,591.8 | \$1,504.7 |
| Discontinued | — | — | — | — | 103.8 |
| Discount department stores | 323.6 | 310.8 | 318.5 | 313.9 | 291.9 |
| Other | 221.1 | 205.4 | 157.6 | 186.4 | 183.8 |
| Total sales | <u>\$2,507.0</u> | <u>\$2,482.5</u> | <u>\$2,369.7</u> | <u>\$2,092.1</u> | <u>\$2,084.2</u> |
| Operating profit (loss): | | | | | |
| Supermarket operations: | | | | | |
| Continuing | \$ 32.4 | \$ 30.9 | \$ 34.7 | \$ 21.0 | \$ 19.4 |
| Discontinued | — | — | — | — | (7.6) |
| Discount department stores | (5.8) | (18.2) | (8.1) | 1.9 | 1.9 |
| Other | .4 | (.5) | 3.5 | 2.2 | 2.3 |
| Total operating profit | <u>27.0</u> | <u>12.2</u> | <u>30.1</u> | <u>25.1</u> | <u>16.0</u> |
| Unallocated expenses: | | | | | |
| Interest | 11.5 | 13.8 | 11.9 | 12.0 | 8.2 |
| Corporate overhead | 5.7 | 5.7 | 5.1 | 5.0 | 4.7 |
| Total unallocated expenses | <u>17.2</u> | <u>19.5</u> | <u>17.0</u> | <u>17.0</u> | <u>12.9</u> |
| Earnings (loss) before income taxes and discontinued operations | | | | | |
| | <u>\$ 9.8</u> | <u>\$ (7.3)</u> | <u>\$ 13.1</u> | <u>\$ 8.1</u> | <u>\$ 3.1</u> |

Consolidated Balance Sheet

Food Fair Stores, Inc. and Subsidiaries

July 31, 1976 and August 2, 1975

ASSETS

| | <u>1976</u> | <u>1975</u> |
|--------------------------------------------------------------------------------------------------------------|----------------------|----------------------|
| Current assets: | | |
| Cash | \$ 16,588,000 | \$ 29,689,000 |
| Marketable securities | 331,000 | 437,000 |
| Accounts receivable, net of allowance for doubtful accounts, \$698,000, 1976; \$1,429,000, 1975 | 20,187,000 | 16,972,000 |
| Inventories | 237,860,000 | 214,770,000 |
| Prepaid expenses | 10,946,000 | 10,611,000 |
| Advances to Fields Credit Corp. (Note 3) | 2,327,000 | 998,000 |
| Refundable income taxes | | 2,723,000 |
| Total current assets | <u>288,239,000</u> | <u>276,200,000</u> |
| Investments (Notes 3 and 4): | | |
| Fields Credit Corp. | 6,432,000 | 6,292,000 |
| Amterre Development Inc. (including advances of \$927,000, 1976; \$1,258,000, 1975) | 7,254,000 | 10,678,000 |
| Other subsidiaries | 6,378,000 | 4,661,000 |
| Miscellaneous | 474,000 | 785,000 |
| | <u>20,538,000</u> | <u>22,416,000</u> |
| Property, plant and equipment: | | |
| Land | 12,127,000 | 12,268,000 |
| Buildings and improvements | 63,795,000 | 61,730,000 |
| Fixtures and equipment | 131,015,000 | 138,231,000 |
| | <u>206,937,000</u> | <u>212,229,000</u> |
| Less accumulated depreciation | 96,790,000 | 94,821,000 |
| | <u>110,147,000</u> | <u>117,408,000</u> |
| Other assets: | | |
| Accounts and notes receivable, not current | 8,175,000 | 5,047,000 |
| Excess of cost over net assets of businesses acquired, net of amortization | 2,056,000 | 1,676,000 |
| Deferred charges | 3,476,000 | 4,614,000 |
| Miscellaneous | 1,711,000 | 1,856,000 |
| | <u>15,418,000</u> | <u>13,193,000</u> |
| | <u>\$434,342,000</u> | <u>\$429,217,000</u> |

Liabilities and Shareholders' Equity

| | <u>1976</u> | <u>1975</u> |
|------------------------------------------------------------------|----------------------|-----------------------------|
| Current liabilities: | | |
| Notes payable (Note 5) | \$ 30,522,000 | \$ 15,098,000 |
| Current portion of long-term debt (Note 5) | 9,119,000 | 6,745,000 |
| Accounts payable | 102,180,000 | 108,546,000 |
| Accrued salaries and other expenses | 39,461,000 | 40,104,000 |
| Income taxes (Note 10) | 4,105,000 | 831,000 |
| Total current liabilities | <u>185,387,000</u> | <u>171,324,000</u> |
| | | |
| Long-term debt, net of current portion (Note 5) | <u>100,903,000</u> | <u>111,033,000</u> |
| Deferred income (Note 6) | <u>1,618,000</u> | <u> </u> |
| Deferred income tax (Note 10) | <u>10,836,000</u> | <u>13,391,000</u> |
| Minority interest in subsidiaries | <u>311,000</u> | <u>322,000</u> |
| | | |
| Commitments and contingencies (Notes 10, 12 and 13) | | |
| Shareholders' equity: | | |
| Preferred stock (Note 7) | 1,960,000 | 2,133,000 |
| Common stock (Note 8) | 7,557,000 | 7,557,000 |
| Capital in excess of par (Note 9) | 51,189,000 | 51,142,000 |
| Retained earnings (Note 5) | 75,898,000 | 73,632,000 |
| | <u>136,604,000</u> | <u>134,464,000</u> |
| Less cost of common shares held in treasury (Note 8) | 1,317,000 | 1,317,000 |
| | <u>135,287,000</u> | <u>133,147,000</u> |
| | <u>\$434,342,000</u> | <u>\$429,217,000</u> |

See notes to consolidated financial statements

Consolidated Statement of

Income (Loss)

Food Fair Stores, Inc. and Subsidiaries

Fifty-two weeks ended July 31, 1976 and August 2, 1975

| | <u>1976</u> | <u>1975</u> |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------|-----------------------|
| Income: | | |
| Sales..... | \$2,507,040,000 | \$2,482,539,000 |
| Equity in earnings of unconsolidated subsidiaries..... | 611,000 | 1,150,000 |
| Gain on debentures purchased for sinking fund..... | 697,000 | 290,000 |
| Other..... | <u>5,622,000</u> | <u>2,302,000</u> |
| | <u>2,513,970,000</u> | <u>2,486,281,000</u> |
| Costs and expenses: | | |
| Cost of sales..... | 2,010,399,000 | 2,006,177,000 |
| Operating, general and administrative expenses..... | 482,258,000 | 473,535,000 |
| Interest..... | <u>11,513,000</u> | <u>13,831,000</u> |
| | <u>2,504,170,000</u> | <u>2,493,543,000</u> |
| Income (loss) from continuing operations | | |
| before income taxes | 9,800,000 | (7,262,000) |
| Income taxes (benefits) (Note 10)..... | <u>3,224,000</u> | <u>(4,036,000)</u> |
| Income (loss) from continuing operations | <u>6,576,000</u> | <u>(3,226,000)</u> |
| Equity in loss of discontinued operations of unconsolidated subsidiary, net of income tax benefit of \$185,000 and \$16,000 in 1976 and 1975, respectively (Note 4)..... | <u>2,748,000</u> | <u>208,000</u> |
| Net income (loss) | <u>\$ 3,828,000</u> | <u>(\$ 3,434,000)</u> |
| Income (loss) per share of common stock: | | |
| Continuing operations..... | \$.88 | (\$.45) |
| Discontinued operations..... | <u>(.37)</u> | <u>(.03)</u> |
| Net income (loss) | <u>\$.51</u> | <u>(\$.48)</u> |

Consolidated Statement of

Retained Earnings

Food Fair Stores, Inc. and Subsidiaries

Fifty-two weeks ended July 31, 1976 and August 2, 1975

| | <u>1976</u> | <u>1975</u> |
|--------------------------------------------------------------------------------------------------------------|----------------------|----------------------|
| Balance, beginning of year, as previously reported | \$ 73,632,000 | \$ 79,996,000 |
| Less adjustment relating to examination of Federal income tax returns by Internal Revenue Service..... | | <u>1,364,000</u> |
| Balance, beginning of year, restated..... | 73,632,000 | 78,632,000 |
| Net income (loss) for the year..... | <u>3,828,000</u> | <u>(3,434,000)</u> |
| | <u>77,460,000</u> | <u>75,198,000</u> |
| Cash dividends paid: | | |
| Preferred stock..... | 89,000 | 91,000 |
| Common stock..... | <u>1,473,000</u> | <u>1,475,000</u> |
| | <u>1,562,000</u> | <u>1,566,000</u> |
| Balance, end of year | <u>\$ 75,898,000</u> | <u>\$ 73,632,000</u> |

See notes to consolidated financial statements.

Changes in Financial Position

Food Fair Stores, Inc. and Subsidiaries

Fifty-two weeks ended July 31, 1976 and August 2, 1975

| | <u>1976</u> | <u>1975</u> |
|-----------------------------------------------------------------|-----------------------|-----------------------|
| Source of funds: | | |
| Net income (loss) for the year | \$ 3,828,000 | (\$ 3,434,000) |
| Items not affecting working capital: | | |
| Depreciation | 17,379,000 | 17,444,000 |
| Amortization | 316,000 | 274,000 |
| Deferred income tax | (2,370,000) | (3,142,000) |
| (Earnings) loss of unconsolidated subsidiaries: | | |
| Continuing operations | (740,000) | (1,135,000) |
| Discontinued operations | 2,748,000 | 208,000 |
| Working capital provided from operations | 21,161,000 | 10,215,000 |
| Disposition of property, plant and equipment | 1,755,000 | 1,570,000 |
| Decrease in investments | | 1,383,000 |
| Increase in long-term debt | 2,030,000 | 7,109,000 |
| Deferred income on sale of computer programs (Note 6) | 1,618,000 | |
| | <u>26,564,000</u> | <u>20,277,000</u> |
| Application of funds: | | |
| Purchase of property, plant and equipment | 11,873,000 | 20,371,000 |
| Decrease in: | | |
| Long-term debt | 12,160,000 | 8,604,000 |
| Lease obligations for closed stores | | 554,000 |
| Increase in: | | |
| Other assets | 2,541,000 | 214,000 |
| Investments | 316,000 | |
| Payment of cash dividends | 1,562,000 | 1,566,000 |
| Purchase of treasury stock | | 670,000 |
| Other changes, net | 136,000 | 148,000 |
| | <u>28,588,000</u> | <u>32,127,000</u> |
| Decrease in working capital | <u>(\$ 2,024,000)</u> | <u>(\$11,850,000)</u> |
| Summary of net changes in working capital: | | |
| Increase (decrease) in current assets: | | |
| Cash | (\$13,101,000) | \$ 3,989,000 |
| Marketable securities | (106,000) | (93,000) |
| Funds held for retirement of bonds | | (6,677,000) |
| Accounts receivable | 3,215,000 | (5,941,000) |
| Inventories | 23,090,000 | (23,544,000) |
| Prepaid expenses | 335,000 | 154,000 |
| Advances to Fields Credit Corp. | 1,329,000 | 15,000 |
| Refundable income taxes | (2,723,000) | 2,723,000 |
| | <u>12,039,000</u> | <u>(29,374,000)</u> |
| Increase (decrease) in current liabilities: | | |
| Notes payable | 15,424,000 | 7,812,000 |
| Current portion of long-term debt | 2,374,000 | (7,178,000) |
| Accounts payable | (6,366,000) | (19,843,000) |
| Accrued salaries and other expenses | (643,000) | 3,460,000 |
| Income taxes | 3,274,000 | (1,775,000) |
| | <u>14,063,000</u> | <u>(17,524,000)</u> |
| Decrease in working capital | <u>(\$ 2,024,000)</u> | <u>(\$11,850,000)</u> |

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements
Years Ended July 31, 1976 and August 2, 1975
1. Summary of significant accounting policies:

Fiscal year: The fiscal year of the Company ends on the Saturday nearest to July 31. Fiscal year 1976 ended July 31, 1976 (52 weeks); fiscal year 1975 ended August 2, 1975 (52 weeks).

Basis of consolidation: The consolidated financial statements include the accounts of the Company and its wholly and majority owned subsidiaries, except the life insurance and credit companies. All significant inter-company balances and transactions have been eliminated. Intercompany profits, if any, in the inventories, are not significant.

Investments in the life insurance and credit companies, 50% owned companies and the common stock of Amterre Development Inc. are stated at the Company's equity in net assets. The investment in the preferred stock of Amterre Development Inc. is stated at cost, equivalent to its liquidating value.

Inventories: Inventories are stated at cost (first-in, first-out or average), which is market or lower. The retail method of accounting is used with respect to inventories of merchandise in stores.

Investments, miscellaneous: Miscellaneous investments are stated at cost.

Property, plant and equipment: Property, plant and equipment are stated at cost. Depreciation for financial reporting purposes is computed on the straight-line method over the estimated useful lives of the assets. For income tax reporting purposes, depreciation is computed by accelerated methods.

Provision for credit losses and charge off policy: Provision for losses on customers' accounts arising from credit sales is made to maintain adequate reserves to cover anticipated losses. Customers' accounts are charged off against the reserve if no payment is received for a stipulated period, or if accounts become uncollectible for other reasons.

Income taxes: Income taxes are provided on all transactions included in the determination of financial income. Where such transactions are included in the determination of taxable income in a different year, such as the acceleration of depreciation and the deferral of gross profit on installment sales, the resulting tax benefits are deferred. Current investment tax credits are being taken into income as the related assets are placed in service.

Other: Debt expense is being amortized over the term of the debentures. If debentures are retired prior to maturity, the unamortized expense is charged to operations.

Excess of cost over net assets of businesses acquired is being amortized and charged against income over a forty-year period.

Pre-opening expenses of J. M. Fields department stores are deferred and charged to operations over a three-year period. With respect to food stores, losses incurred in the initial three months by new stores, remodeled stores, and stores converted to discount operations are deferred and amortized over a three-year period.

Pension plans: Pension expense includes normal cost and amortization of prior service costs over a forty-year period. The Company's policy is to fund pension costs accrued.

Net income (loss) per common share: Net income (loss) per common share is based on the weighted average number of shares outstanding during the years. Warrants and convertible subordinated notes have no dilutive effect.

2. Reclassification: The financial statements for fiscal 1975 have been reclassified to conform with the presentation for 1976.

3. Investment, Fields Credit Corp.: Fields Credit Corp. purchases the revolving credit and installment sales accounts of J. M. Fields, Inc. The accounts are transferred with recourse and, accordingly, bad debt losses are recorded in the accounts of J. M. Fields, Inc. During the current year J. M. Fields, Inc. discontinued installment sales and revolving charge account sales. It is anticipated that the balance of customer receivables will be collected over a maximum of twenty-four months. Pretax earnings of \$269,000 in 1976 and \$190,000 in 1975 have been included in the consolidated statement of income as a reduction of interest expense and the related income taxes are included in the taxes on income. Summary financial information for Fields Credit Corp. is as follows:

**Balance sheet at July 31, 1976
and August 2, 1975:**

| | 1976 | 1975 |
|-----------------------------------------------------------------|-----------------|-----------------|
| | (in thousands) | |
| Assets | | |
| Cash | \$ 150 | \$ 133 |
| Due from J. M. Fields, Inc. | 283 | 1,187 |
| Customers' receivables | 22,205 | 34,669 |
| Unearned income | (364) | (695) |
| Allowance for doubtful accounts | (328) | (510) |
| | <u>\$21,946</u> | <u>\$34,784</u> |
| Liabilities and Equity | | |
| Notes payable, banks | \$13,000 | \$27,200 |
| Advances from Food Fair Stores, Inc. | 2,327 | 998 |
| Accrued expenses | 187 | 294 |
| Subordinated notes payable to Food Fair Stores, Inc. | 5,900 | 5,900 |
| Equity of Food Fair Stores, Inc. | 532 | 392 |
| | <u>\$21,946</u> | <u>\$34,784</u> |

**Operations for fifty-two weeks
ended July 31, 1976 and
August 2, 1975:**

| | 1976 | 1975 |
|------------|-----------------|-----------------|
| | (in thousands) | |
| Revenues | <u>\$ 4,229</u> | <u>\$ 6,017</u> |
| Net income | <u>\$ 140</u> | <u>\$ 99</u> |

4. Investment, Amterre Development Inc. (Amterre):

The Company owns all of the preferred stock and 40% of the common stock of Amterre. At July 31, 1976 the value of the preferred stock was \$2,000,000 (Note 1), and the market value of the common stock was \$2,916,000 based on a quoted bid price of \$.875 per share.

Condensed financial statements of Amterre are as follows:

| Consolidated balance sheet: | December 31, | |
|----------------------------------------------------------------------------|------------------|------------------------|
| | 1975 | 1974 (reclassified) |
| | (in thousands) | |
| Assets | | |
| Property and equipment, at cost, net of accumulated depreciation | \$182,450 | \$181,652 |
| Net property and related assets in process of disposition | 60,245 | 62,295 |
| Less: | | |
| Related mortgages and other liabilities | (48,857) | (48,558) |
| Provision for loss on disposition | (11,388) | |
| | <u>—0—</u> | <u>13,737</u> |
| Other assets | 11,451 | 9,325 |
| | <u>\$193,901</u> | <u>\$204,714</u> |
| Liabilities and Equity | | |
| Notes, mortgages and debentures payable | \$172,442 | \$170,844 |
| Construction loans payable | 4,141 | 3,731 |
| Other | 4,498 | 9,585 |
| | <u>181,081</u> | <u>184,160</u> |
| Shareholders' equity | 12,820 | 20,554 |
| | <u>\$193,901</u> | <u>\$204,714</u> |

| Consolidated statement of income: | Year ended December 31, | |
|---------------------------------------------------------------------------------|----------------------------|------------------------|
| | 1975 | 1974 (reclassified) |
| | (in thousands) | |
| Income | \$27,474 | \$27,401 |
| Expenses, net | 27,892 | 26,456 |
| Income (loss) from continuing operations before income taxes (418) | | 945 |
| Income taxes (benefit) (137) | | 325 |
| Income (loss) from continuing operations (281) | | 620 |
| Loss from discontinued operations, net of income tax benefit (7,333) | | (560) |
| Net income (loss) | <u>(\$7,614)</u> | <u>\$60</u> |

Net property and equipment and related assets in process of disposition and the loss from discontinued operations relate to the Gateway Urban Renewal Project in Newark, New Jersey. Effective April 1, 1976, the property was transferred to the mortgagee in satisfaction of the first mortgages on the properties.

The Company's equity in the loss on disposition of the Gateway Project, \$2,748,000 net of applicable income tax benefits, is reported in the statement of income (loss) under the caption "Equity in loss from discontinued operations of unconsolidated subsidiary."

The Company's equity in Amterre's income (loss) from continuing operations was (\$160,000) in 1976 and \$200,000 in 1975, which amounts are included in the caption "Equity in earnings of unconsolidated subsidiaries" and have been adjusted to provide for dividends paid on preferred stock of \$120,000 in each year.

The Company is obligated to Amterre under 96 leases expiring through 2057. The minimum annual rentals applicable to such leases have been included in the lease obligations set forth in Note 13.

In 1976, the Company credited income with \$135,000 net of applicable income taxes, representing consideration to the Company for the relinquishment of lease rights to certain parcels of land sold by Amterre. At July 31, 1976, Amterre was indebted to the Company for an aggregate of \$927,000 for advances and mortgages.

5. Indebtedness:

| | Rate | Amount (in thousands) | Maturity |
|------------------------------------------|------------------------|--------------------------|-----------|
| Notes: | | | |
| Banks | 7% to 116% of prime | \$ 21,296 | 1977-1980 |
| Other | 5%-9% | 6,632 | 1976-1984 |
| Mortgages | 4.75%-10.5% | 16,234 | 1977-2001 |
| Convertible subordinated notes | 4% | 480 | 1977 |
| Subordinated debentures | 4% | 11,941 | 1979 |
| Subordinated notes | 8.5% | 21,000 | 1984 |
| Sinking fund debentures | 8.375% | 32,439 | 1996 |
| | | <u>110,022</u> | |
| Less current portion | | 9,119 | |
| | | <u>\$100,903</u> | |

Convertible subordinated notes (4%) are convertible into common stock at \$24.01 per share through May 12, 1977 and require annual principal payments of \$480,000.

Subordinated debentures (4%) require annual sinking fund payments of \$967,000.

Subordinated notes (8.5%) require annual payments of \$2,000,000.

Sinking fund debentures (8.375%) require annual sinking fund payments of \$1,750,000 commencing January 15, 1977. The sinking fund requirements for the year ending July 30, 1977 have been anticipated.

The indentures covering the issuance of the debentures and notes described above contain restrictions as to the payment of cash dividends, the redemption of shares of stock of the Company, working capital and shareholders' equity. The maximum amount of retained earnings so restricted was \$63,544,000 and \$64,211,000 at July 31, 1976 and August 2, 1975, respectively.

5. Indebtedness (continued):

At July 31, 1976 the Company had lines of credit available from various banks totalling \$61,700,000 at the prevailing prime interest rate; of this amount, \$30,600,000 was unused. These lines are supported by the Company's normal cash balances maintained on a daily basis and there is no legal restriction on the availability of such balances. During fiscal 1976, short-term borrowings averaged approximately \$28,600,000 (maximum \$40,000,000) at an average interest rate of 7.2%.

6. Deferred income: On May 7, 1976, the Company sold all its data processing programs and certain computer equipment to RMC Group, Inc. (RMC), a company which has managed the Company's electronic data processing operations for the past two years. The equipment and computer programs acquired by RMC will also be utilized to provide similar services to third parties. The consideration consisted of a cash payment of \$200,000 and RMC's non-recourse promissory note secured by the equipment and programs in the principal amount of \$1,600,000, payable over seven years with interest at the rate of 7% per annum. The Company has entered into an agreement with RMC to manage and operate its computer operations for a period of seven years. It is expected that fees to be paid by Food Fair Stores, Inc. for these services will be less than the costs which would be incurred in operating its own computer department.

RMC granted to the Company an option, exercisable after January 14, 1979 and until November 8, 1979, to acquire, for \$1,000,000, a 40% stock interest in RMC.

The aggregate gain on the sale of the programs and equipment, \$1,680,000, has been deferred and will be credited to income over the term of the management agreement. In 1976, \$31,000, net of applicable income taxes, is included in the statement of income with respect to this transaction.

7. Preferred stock: Preferred stock is \$4.20 cumulative, \$15 par (stated at liquidating value of \$100 per share); 108,190 shares are authorized, of which 19,601 and 21,328 are outstanding at July 31, 1976 and August 2, 1975, respectively. The Company is obligated to set aside \$120,000 semi-annually as a sinking fund for the redemption of the preferred stock, which may be called for this purpose at \$100 per share plus accrued dividends.

8. Common stock: Common stock is \$1 par; 10,000,000 shares are authorized, of which 7,557,378 are issued. Shares acquired for the treasury are 196,577 at July 31, 1976 and August 2, 1975.

At July 31, 1976 warrants to purchase 416,160 shares of common stock were outstanding. These warrants are exercisable at \$23.05 per share and expire December 17, 1979.

9. Capital in excess of par: The increase in capital in excess of par during the years ended July 31, 1976 and August 2, 1975 represents the excess of stated value over cost of cumulative preferred stock retired.

10. Income Taxes: The provision for income taxes or tax benefits is comprised of the following:

| | 1976 | 1975 |
|---------------------------------|----------------|------------------|
| | (in thousands) | |
| Federal: | | |
| Current | \$2,722 | (\$1,232) |
| Deferred | 783 | (3,127) |
| Investment tax credit | (994) | |
| State | 713 | 323 |
| | <u>\$3,224</u> | <u>(\$4,036)</u> |

A reconciliation of income taxes or benefits on income (loss) from continuing operations in 1976 and 1975 with the amount computed at the Federal income tax rate of 48% is as follows:

| | 1976 | 1975 |
|-------------------------------------------------------------------------------------------------------------|----------------|------------------|
| | (in thousands) | |
| Computed "expected" income tax expense (benefits) at 48% | \$4,704 | (\$3,486) |
| State income taxes, net of Federal tax effect | 371 | 168 |
| Tax benefit from: | | |
| Income taxed at capital gains rate | (381) | |
| Dividend income not taxable | (66) | (50) |
| Investment tax credit | (994) | (1,172) |
| Net earnings of unconsolidated subsidiaries taxed at reduced rates | (250) | (55) |
| Tax effect of nontaxable items included in income of prior years affected by carryback adjustment | | 484 |
| Other items, net | (160) | 75 |
| Income tax (benefits) on income from continuing operations | <u>\$3,224</u> | <u>(\$4,036)</u> |

For the fiscal year 1975, unused investment tax credits available for financial reporting purposes at August 2, 1975 (\$3,500,000) were applied in reduction of deferred income taxes.

The Company and its subsidiaries file a consolidated Federal income tax return. At July 31, 1976, the Company has available for Federal income tax purposes investment tax credit carryforwards of approximately \$5,000,000. These tax credit carryforwards expire as follows:

| Fiscal Year | Amount (in thousands) |
|-------------|--------------------------|
| 1979 | \$1,200 |
| 1980 | 1,700 |
| 1981 | 900 |
| 1982 | 1,200 |
| | <u>\$5,000</u> |

The Federal income tax returns of the Company and certain subsidiaries have been examined by Internal

Revenue Service for the fiscal years 1964 through 1968. The service has proposed adjustments which would result in additional taxes of approximately \$6,200,000 exclusive of interest. Since the material issues may be litigated, it is not presently possible to estimate the ultimate outcome of the tax controversies.

11. Pension plans: The Company and its subsidiaries have several noncontributory pension plans covering certain hourly and salaried employees. Pension expense for the years ended July 31, 1976 and August 2, 1975 was \$1,287,000 and \$1,201,000, respectively. The actuarially computed value of vested benefits for certain plans at January 1, 1976 exceeded the fund assets and balance sheet accruals by approximately \$2,801,000.

12. Contingencies: The Company has been named a defendant in six civil actions brought by members of the cattle ranching industry charging violations of the anti-trust laws in the purchase and sale of meat. The complainants seek damages in an unspecified amount and an injunction against further anti-trust violations as alleged. Management believes that no basis exists for the allegations made against the Company in these complaints.

The Company is party to various other claims and lawsuits arising in the normal course of business. In the opinion of management, the outcome of the various actions will not materially affect the Company's consolidated income or financial position.

The Company is contingently liable at July 31, 1976, for accounts receivable aggregating \$10,716,000 sold to a bank with recourse.

13. Leases: At July 31, 1976, the Company was lessee under leases covering principally retail locations and distribution centers. Realty lease terms generally range to twenty-five years, with options of renewal for additional periods. Equipment leases expire at various dates through 1985.

For purposes of the following disclosure, the Company has made a distinction between financing lease arrangements and other lease arrangements. Total rental expense, net of sublease rental income, for the years ended July 31, 1976 and August 2, 1975 was as follows:

| | 1976 | 1975 |
|----------------------------------|-----------------|-----------------|
| | (in thousands) | |
| Financing leases: | | |
| Minimum rentals | \$22,020 | \$22,274 |
| Rentals based on sales | 452 | 497 |
| Sublease rentals | (2,577) | (1,956) |
| | <u>19,895</u> | <u>20,815</u> |
| Other leases: | | |
| Minimum rentals | 14,870 | 14,764 |
| Rentals based on sales | 1,422 | 1,715 |
| Sublease rentals | (886) | (572) |
| | <u>15,406</u> | <u>15,907</u> |
| Total rent expense | <u>\$35,301</u> | <u>\$36,722</u> |

Rental expense for financing leases includes payments to unconsolidated affiliated real estate companies of \$13,504,000 and \$14,081,000 in 1976 and 1975, respectively.

Minimum rental commitments, exclusive of taxes and other costs paid by the Company, are approximately as follows for the fiscal years indicated.

| Years | Net all leases | Financing leases | Other leases | Sublease rental income | |
|----------------|------------------|------------------|------------------|------------------------|------------------|
| | | | | Financing leases | Other leases |
| (in thousands) | | | | | |
| 1977 | \$ 33,281 | \$ 22,008 | \$ 14,221 | (\$2,068) | (\$880) |
| 1978 | 32,599 | 21,891 | 13,446 | (1,919) | (819) |
| 1979 | 31,837 | 21,865 | 12,462 | (1,749) | (741) |
| 1980 | 30,502 | 21,480 | 11,160 | (1,539) | (599) |
| 1981 | 28,435 | 20,300 | 9,793 | (1,229) | (429) |
| 1982-1986 | 110,543 | 83,786 | 31,994 | (3,879) | (1358) |
| 1987-1991 | 73,074 | 57,545 | 17,728 | (1,713) | (486) |
| 1992-1996 | 44,427 | 41,610 | 3,924 | (1,041) | (66) |
| Thereafter | 16,431 | 10,343 | 6,244 | (156) | — |
| | <u>\$401,129</u> | <u>\$300,828</u> | <u>\$120,972</u> | <u>(\$15,293)</u> | <u>(\$5,378)</u> |

The present value of the minimum lease commitments for financing leases was \$180,158,000 at July 31, 1976 and \$191,621,000 at August 2, 1975, based on calculations using interest rates ranging from 4.25% to 11.75%. The weighted average interest rates were 7.00% and 6.96% for 1976 and 1975, respectively.

If, instead of recording rental expense, all financing leases were capitalized, related assets were amortized on a straight-line basis and interest costs were accrued on the basis of outstanding lease liability, the effect on net income would be as follows:

| | 1976 | 1975 |
|----------------------------------------|----------------|---------------|
| | (in thousands) | |
| Amortization of lease rights | \$11,171 | \$11,141 |
| Interest costs | 12,858 | 13,422 |
| | <u>24,029</u> | <u>24,563</u> |
| Rental expense | 22,472 | 22,771 |
| | <u>1,557</u> | <u>1,792</u> |
| Allocated income taxes | 747 | 860 |
| Increase in expense | <u>\$ 810</u> | <u>\$ 932</u> |

14. Transactions with certain parties: The Company is obligated to an affiliated real estate company under 136 leases expiring through 1991. The minimum annual rentals applicable to such leases have been included in the lease obligations set forth in Note 13. At July 31, 1976, advances to the affiliate of \$2,915,000, plus the accrued interest thereon, have been included as accounts receivable, not current.

The Company is obligated to Hasam Realty Corp., a major stockholder of the Company, under two store leases which expire in 1990. The leases provide for minimum annual rentals of \$276,000, exclusive of taxes, insurance and other expenses.

14. Transactions with certain parties (continued):

During 1976, in connection with the reorganization in Chapter XI of Filigree Foods, Inc. (Filigree), a wholesale grocery company which had previously serviced the Company's supermarkets in the North Jersey area, Hasam Realty Corp. (Hasam) acquired 570,331 shares of common stock of Filigree, equal to a 49% interest, for an investment of \$500,000, and warrants to acquire an additional 116,394 shares of Filigree common, equal to a 10% interest. Hasam granted to the Company an option, exercisable until April, 1977, to acquire Hasam's interest in Filigree for an amount equal to Hasam's investment plus carrying costs. Filigree's bank lenders required Filigree to obtain the Company's agreement that in the event of future default by Filigree on its bank loans, the Company would bid, at any foreclosure of Filigree's grocery inventory, an amount equal to 50% of the wholesale cost thereof, up to a maximum of \$1,500,000. Hasam has agreed to indemnify the Company in event it were to purchase such merchandise, and has additionally transferred to the Company in consideration of such undertaking warrants to acquire 58,197 shares of Filigree common stock. Should the Company exercise its option to acquire Hasam's interest in Filigree, Hasam will also transfer to the Company, without additional consideration, Hasam's remaining common stock purchase warrants.

15. Subsequent event: On October 2, 1976, the Company took possession of 17 supermarkets formerly owned by Penn Fruit Co., Inc. and is currently operating 14 of such supermarkets, all pursuant to an agreement previously made for the sale to the Company of such supermarkets.

STOCK PRICE DATA

The following table indicates the high and low sales prices of the Company's common stock on the New York Stock Exchange for the fiscal quarters indicated.

| | FOURTH | THIRD | SECOND | FIRST |
|-------------|--------|-------|--------|-------|
| 1976 | | | | |
| High | 6 | 6½ | 5½ | 5 |
| Low | 5¼ | 5 | 4 | 4 |
| 1975 | | | | |
| High | 5¾ | 6¼ | 6 | 6¼ |
| Low | 4% | 4¾ | 3¾ | 4½ |

A cash dividend of 5¢ a share was paid in each of the calendar quarters.

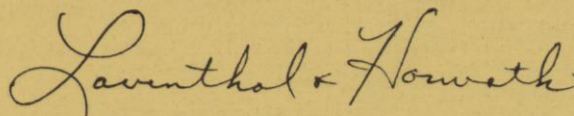
The Board of Directors and Shareholders
Food Fair Stores, Inc.

We have examined the consolidated balance sheet of Food Fair Stores, Inc. and Subsidiaries as at July 31, 1976 and August 2, 1975 and the related consolidated statements of income (loss), retained earnings and changes in financial position for the fifty-two week periods then ended. Our examination was made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

The opinion in our report dated October 20, 1975 on the Company's 1975 consolidated financial statements was qualified with respect to the uncertainty as to the realization of the Company's investment in Amterre Development Inc. Because of developments described in Note 4, the qualification of our opinion as to this matter is removed.

As described in Note 10, the Federal income tax returns of the Company and certain subsidiaries have been examined by Internal Revenue Service for the fiscal years 1964 through 1968. The Service has proposed adjustments which would result in additional taxes of approximately \$6,200,000, exclusive of interest. Since the material issues may be litigated, it is not presently possible to estimate the ultimate outcome of the tax controversies.

In our opinion, subject to the effects of the tax matter discussed in the preceding paragraph, the aforementioned financial statements present fairly the consolidated financial position of Food Fair Stores, Inc. and Subsidiaries at July 31, 1976 and August 2, 1975 and the consolidated results of their operations and changes in their financial position for the fifty-two week periods then ended, in conformity with generally accepted accounting principles applied on a consistent basis.



Philadelphia, Pa.
October 20, 1976

Executive Offices 3175 John F. Kennedy
Blvd., Philadelphia, Pa. 19101

General Counsel Stein Rosen & Ohrenstein,
1370 Avenue of the Americas, New York,
N.Y. 10019

Transfer Agent Registrar & Transfer
Company, 34 Exchange Place, Jersey
City, N.J. 07302

Registrar The Chase Manhattan Bank N.A.,
1 Chase Manhattan Plaza, New York,
N.Y. 10015

Certified Public Accountants Lavenenthal &
Horwath, 1845 Walnut Street,
Philadelphia, Pa. 19103

DIRECTORS

| | |
|--------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Willard S. Boothby, Jr. | Chairman & Chief Executive Officer of Blyth Eastman Dillon & Co., Inc. |
| William P. Davis, III | Chairman of the Audit Committee Vice President for University Relations, Drexel University Chairman of the Executive Committee of First Pennsylvania Bank, N.A. |
| George Friedland | Retired Vice Chairman |
| Harold Friedland | Vice President |
| Jack Friedland | President |
| Samuel Friedland | Chairman of the Executive Committee |
| Hess Kline | Chairman of George Allen Inc. |
| Samuel P. Mandell | Investor |
| Arthur S. Rosenberg | Retired Senior Vice President |
| Herman R. Silver | Retired Vice President |
| Louis Stein | Chairman of the Finance Committee Investor |
| W. Paul Stillman | Chairman of the Compensation Committee Chairman The First National State Bank of New Jersey The First National State Bancorporation, Newark, N.J. The Mutual Benefit Life Insurance Co. |

CORPORATE OFFICERS

| | |
|----------------------------|----------------------------------------------------------------|
| Jack Friedland | President Chief Executive Officer |
| J.A. Berger | Vice President Director of Manufacturing & Food Processing |
| Harold Friedland | Vice President |
| Frank N. James | Vice President President, Pantry Pride Supermarket Division |
| J. Arvid Jonsson | Vice President Director of Industrial Relations |
| S. Robert Silverman | Vice President Director of Distribution |
| Leo Dicandilo | Treasurer |
| Howard F. Gordon | Secretary |
| Franklin A. Gaber | Assistant Treasurer |
| Edmond O'Neill | Assistant Secretary |
| Harvey Richards | Assistant Secretary |
| Leonard Stubins | Assistant Secretary |

DIVISIONAL OFFICERS

Pantry Pride Supermarket Division

| |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| President Frank N. James |
| Executive Vice President Marvin Lerner |
| Vice Presidents Herbert Carlis David Epstein Seymour I. Friedman Jack Marcus Jack Miller Jack Millman Edwin Segal Jack Silverman Sheldon B. Sosna Beryl Weinstein Herbert Zandler |
| Assistant Vice Presidents Sidney Beck Albert Faraldi Robert U. Ochsenhirt Ronald Stubin Robert Wein |

Tulip Construction Division

| |
|------------------------------------------------------------------|
| Senior Vice President Marvin Kushner |
| Tulip Real Estate Division |
| Senior Vice President Sidney Tucker |
| Vice President Clarence J. MacManus |
| J.M. Fields, Inc. |
| Senior Vice Presidents Ralph Blumenstock Robert M. Hunt |
| Vice Presidents Oscar Kettler Jack Rule Howard Siegrist |
| Treasurer John R. Johnson |

Ideal Shoe Company

| |
|------------------------------------------|
| President Leonard Pasternak |
| Senior Vice President Alexander Aezen |
| Vice President Harry Haber |

Washington Square Life Insurance Co.

| |
|---------------------------------|
| President Jay Gross |
| Vice President Jerome Brandt |
| Treasurer Ronald Funk |

MGS Incentives Company

| |
|------------------------------|
| President Harold H. Rubin |
|------------------------------|

Designed & illustrated by Kay B. Gill
Creative Director—Anthony M. Russo

Food Fair Stores, Inc.
3175 John F. Kennedy Blvd., Philadelphia, Pa. 19101

